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FEDERAL COMMUNICATIONS COMMISSION
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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

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In the Matter of	)	
	)	
Federal-State Joint Board on Universal Service	)	CC Docket No. 96-45
	)	
	)	

COMMENTS

TELEPORT COMMUNICATIONS GROUP INC.

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December 19, 1996

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SUMMARY

TCG supports the Joint Board's overall recommendations for both the high cost fund and the fund for schools and libraries. TCG does suggest certain limited modifications or clarifications to those recommendations, to better comport with the overall objectives of the Act.

TCG believes that universal service support should not be extended to single-line businesses. Businesses, no matter what size, are better able than residential consumers to pay the full cost of their service -- after all, businesses must pay rent, salaries, taxes, electric rates, and other costs of operation. TCG therefore recommends that the FCC modify the Board's definition and limit support to residential customers who have low incomes or who live in high cost areas.

TCG strongly supports competitive bidding as a fundamental prerequisite to a "bona fide request" for support by schools and libraries. TCG is concerned, however, that the Board's recommendation would weaken, if not nullify, that requirement by permitting existing contracts to remain in place. Schools and libraries that have contracted with the ILECs without entertaining bids from other providers should be required to reopen those contracts to bidding if their carrier is to receive support. As for the RFPs themselves, TCG recommends that bidding for support-eligible contracts be limited to one round of sealed bids, to reduce the burden on schools and libraries and encourage "best behavior" on the part of carriers.

Finally, in establishing the criteria for an exemption for *de minimis* contributions to the fund, the costs of complying with the contribution requirements should be considered. If a small carrier's cost of complying with the universal service rules exceeds the amount of its contribution, it makes sense to classify those contributions as *de minimis* and to exempt that carrier from contributing.

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COMMENTS OF TELEPORT COMMUNICATIONS GROUP INC.

Teleport Communications Group Inc. ("TCG") hereby offers the following comments in response to the Commission's request for comments in the above-captioned proceeding. TCG's comments are organized according to the format of the Joint Board's Recommended Decision.

I. INTRODUCTION.

TCG has been a leader in seeking real solutions to the question of how to maintain and advance universal service under competition. In 1993, TCG proposed replacing the alleged system of implicit universal service subsidies with an explicit fund, administered by a neutral third party, supported by all telecommunications service providers, and available to all carriers providing service to support-eligible customers. The 1996 Telecommunications Act, and the Recommended Decision issued by the Federal-State Joint Board, echo many of the principles that TCG has advocated. The Act and Recommended Decision seek to guarantee that universal service will be advanced and maintained in a manner not only compatible with competition, but in a way that takes advantage of market forces to bring more choices and better quality to all consumers at affordable prices.

TCG therefore supports the Joint Board's overall recommendations for both the high cost fund and the fund for schools and libraries. TCG does suggest certain limited modifications or clarifications to those recommendations, to better comport with the overall objectives of the Act. With these modifications, the Board's recommendations will help put an end to the false ILEC claims that competition will adversely impact universal service, and show instead that competition and universal service go hand-in-hand.

TCG commends the Federal-State Joint Board for its many months of hard work on this difficult and complex topic. TCG appreciates this opportunity to comment on the Board's recommendation and looks forward to working with both the Board and the Commission in the coming months to implement this innovative approach to universal service.

II. DISCUSSION.

A. Principles.

TCG strongly supports the Board's recommendation to add competitive neutrality to the list of fundamental principles of universal service enumerated in the Act. The future of universal service, like the future of telecommunications in general, is grounded in competition. All customers, subsidized or not, should no longer have to depend exclusively on monopolies for local telephone service. No carrier should look upon universal service as either an exclusive right or as a unique burden. Adherence to this principle will ensure that all carriers will make equitable contributions to the universal service mechanism and that all eligible carriers will have equal access to universal service support on behalf of their high cost or low income customers.

B. Definition of Services.

TCG has long supported the specification of a package of telecommunications services that will ensure a basic level of connectivity to the public switched telecommunications network for all consumers. TCG believes that the package of support-eligible services proposed by the Joint Board is appropriate and urges the Commission to adopt it.

TCG disagrees, however, with the Board's recommendation to extend support for this service package to single-line businesses,[1] for several reasons. First, businesses, no matter what size, are better able than residential consumers to pay the full cost of their service.[2] Businesses, after all, must pay rent, salaries, taxes, electric rates, and other costs of operation. Second, there is no evidence to suggest that businesses are unable to pay cost-based rates for their service or that any would cancel service if they had to pay cost-based rates. Third, the Commission has not tracked business subscription levels historically, nor have

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[1] *See* Recommended Decision, paragraph 91.

[2] The Joint Board acknowledged this fact when it proposed that business support, to the extent it was determined to be necessary, would be based on a higher benchmark than residential service support (Paragraph 92 of Recommended Decision).

business consumers been considered covered by the universal service umbrella in the past. There is no indication from the Act that they should be eligible for support in the future. Lastly, businesses are more likely to reap the benefits of competition and choice sooner than residential customers. TCG therefore recommends that the FCC modify the Board's definition and limit support to residential customers who have low incomes or who live in high cost areas.

C. Service Area.

The service area requirement of Sec. 214(e) of the Act is an important element in ensuring that universal service is administered in a competitively neutral manner. If the service area is too large (i.e., existing ILEC study areas), a new entrant will find itself at a distinct disadvantage relative to the incumbent carrier whose network is already in place. In that case, the new entrant may not be able to serve a territory large enough to qualify it as a recipient of universal service support -- especially on a facilities basis -- while the incumbent can receive such support because its facilities are already in place. This disadvantage may be so great as to discourage the new entrant from entering the market at all.

Although Sec. 214(e) of the statute quite clearly states that the responsibility for establishing the service territory rests with the states (and the Board's recommendation appears to recognize the states' important role), the Commission is free to provide the states with well-reasoned guidelines. TCG urges the Commission to adopt stronger guidelines for the states to follow regarding the size of the service area to be served by eligible carriers.[3] TCG recommends that service areas should be consistent with the cost study parameters eventually adopted by the Commission. Both the "BCM2" and the "Hatfield" models estimate costs at the Census Block Group level (although both have been criticized for ignoring existing wire center boundaries), areas far smaller than the traditional LEC "study areas." Additionally, service areas should not be so large as to violate the principle of competitive neutrality or the federal statute's prohibition on barriers to entry. Accordingly, and regardless of which geography the Commission ultimately adopts for cost study purposes (CBG, wire center, or some combination of the two), carriers should not be required to serve any territory larger than that used for the cost study, or any area that would confer an unfair competitive advantage on any carrier.

D. Rural, Insular, and High Cost Areas.

Proxy Models

TCG agrees that the proxy models submitted in this proceeding are deficient in a number of respects (e.g., poorly documented, not consistent with economic cost principles), and recommends that the Commission carefully consider the independent analysis of the "BCM2" and "Hatfield" models by Dr. David Gabel for the National Regulatory Research Institute. Among the most serious of Dr. Gabel's conclusions is that neither model adheres to Total Service Long Run Incremental Cost ("TSLRIC") principles. That is, neither model estimates the costs that would

[3] *See* Recommended Decision, paragraph 175.

be avoided if a provider stopped offering basic service yet continued to offer all of its other services to all of its other customers. By failing to comply with this fundamental principle of forward-looking cost methodology, both of these models appear to have significantly overestimated the cost of basic service and the size of the universal service fund. TCG hopes that the workshops scheduled to begin in January will address these concerns and result in a model that comports with the cost principles of the Joint Board.[4]

Benchmarking

TCG strongly supports the Board's recommendation to calculate the subsidy requirement as the difference between total revenue per line and the TSLRIC of those services, rather than the difference between basic service rates and the TSLRIC of basic service.[5] Such an approach is simply common sense and recognizes the fact that telephone subscribers buy much more than basic service and generate far more revenue for their local service provider than the rates for flat rate service and the Subscriber Line Charge. Indeed, to the extent that rates for basic service do not cover the cost of basic service (TSLRIC or embedded), the shortfall may be more than overcome by profits from discretionary services. The basic service rates, therefore, are no more than a "loss leader" for the provider, used to attract the customer so that the provider can sell the customer other, more profitable products and services.

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[4]*See* Recommended Decision, paragraph 277.

[5]*See* Recommended Decision, paragraphs 310-311.

It is also important to realize that these discretionary services (e.g., call forwarding, call waiting, call answering) can be provided to that customer only by the customer's basic service provider. That is, once a customer selects a local service provider, that provider has captured the *exclusive* right to sell that customer additional services.[6] The Board has correctly recognized, therefore, that subscribers to basic service are much more valuable to their carriers than the rates for basic service would imply, and that such revenue opportunities should be taken into account when calculating the support requirement.

It is worth noting, as well, that once all the relevant revenue is accounted for, the universal service "problem" may prove to be much more manageable than anticipated. As was noted above, proper TSLRIC cost models would likely show a much lower cost associated with the provision of basic service than the current proxy models, and would therefore require a much smaller universal service support fund. Similarly, if all relevant revenue (i.e., revenues from both basic and discretionary services) is properly accounted for, the Commission might discover that revenue exceeds even embedded costs, as well as TSLRIC. TCG believes, therefore, that the Joint Board has established the proper framework and principles to accurately calculate the true universal service challenge and strongly encourages the Commission to adopt the benchmarking recommendation.

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[6]Unlike loss leaders offered by, for example, grocery stores, telephone subscribers have no alternatives once they select their basic service provider. A grocery store customer at least has the option to go to another store for his other purchases once he has purchased the loss leader item.

E. Schools and Libraries.

TCG strongly supports competitive bidding as a fundamental prerequisite to a "bona fide request" for support.[7] TCG is concerned, however, that the recommendation appears to weaken -- indeed, to nullify --that requirement by permitting existing contracts to remain in place.[8] Although in some instances existing contracts have been awarded via competitive bidding, the nascent state of competition guarantees that most existing contracts were awarded in the past to the incumbent local exchange carrier by default. If such contracts are permitted to remain in place, competitors will be effectively barred from potentially lucrative markets and the schools and libraries will remain captives of the incumbent monopolists. Schools and libraries that have contracted with the ILECs without entertaining bids from other providers, therefore, should be required to reopen those ILEC contracts to bidding if their carrier is to receive support. The Board's innovative recommendation to initiate Requests for Proposals ("RFP") via an Internet web page will minimize any burden the schools and libraries may shoulder as they take advantage of their new freedoms. Their efforts will be well rewarded by the new competitive marketplace for local telecommunications services.[9]

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[7]*See* Recommended Decision, paragraph 539.

[8]*See* Recommended Decision, paragraph 572.

[9]Given the limited state of competition today and in the near future, however, it is unlikely that every RFP will elicit a competitive response. In those instance where contracts are awarded to the incumbent local exchange carrier by default, those contracts must be for a term of no more than three years.

As for the RFPs themselves, TCG recommends that bidding for support-eligible contracts be limited to one round of sealed bids. Such an approach will not only minimize the burdens on the schools and libraries, but it will also encourage "best behavior" on the part of carriers. Auctions, as was thoroughly discussed by the Joint Board, are complicated undertakings requiring substantial oversight to prevent "gaming" and to ensure fair treatment of all parties. The best way to minimize the problems associated with an RFP is to encourage the bidders to make their first offer their best offer. It has been TCG's experience in arbitration proceedings, for example, that when forced to make a best and final offer, carriers do so, and that this produces a faster, less expensive, and more efficient resolution than more complicated procedures. A single sealed bid will similarly simplify the school's decision so that teachers and students can take advantage of the services as quickly as possible. Multiple rounds of bidding, by contrast, would delay the process and will only encourage gamesmanship on the part of the bidders as they use the RFP simply as a means of obtaining information about their competitors.

TCG supports the concept of a discount matrix,[10] but agrees that the cost dimension of the affordability matrix needs to be defined better: i.e., what constitutes a high cost area. The proxy models should provide an adequate indication of the relative costs of serving one area versus another and TCG recommends their use for this purpose.

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[10] *See* Recommended Decision, paragraph 555.

Finally, TCG agrees with the Board's recommended criteria for a bona fide request for support:[11] (1) a formal plan by the school ; (2) an RFP posted on the fund administrator's website; and (3) an affidavit by a school authority verifying the educational intents and purposes of the services to be purchased. These three criteria and the requirement that all schools pay at least a portion of the cost of the service will ensure that the funds are spent wisely and where they are most needed, and mitigate any concern that the promise of "free" money to buy attractive new telecommunications services might encourage unnecessary purchases simply because the money appears to be readily available.

F. The Subscriber Line and Carrier Common Line Charges.

TCG agrees that Long Term Support ("LTS") is an implicit subsidy within the access charge regime. Because the new universal service mechanism will address the high loop costs that have been the target of LTS payments, LTS should be removed from the Carrier Common Line Charge ("CCLC"). TCG hopes that the new universal service fund will constrain the growth of long term support which stood at $329 million only two years ago and is now over $405 million.

As for the Subscriber Line Charge ("SLC") and the remainder of the Carrier Common Line Charge, TCG reiterates its position that neither the SLC nor the CCLC are universal service mechanisms, and therefore should not be addressed here. In doing so, TCG agrees with Commissioner Chong that the SLC and the

[11] *See* Recommended Decision, paragraphs 600-603.

CCLC will be better addressed in the access charge reform docket, not the universal service docket.

G. Administration.

Contribution

TCG disagrees with the Board's recommendation to disregard a carrier's cost of complying with the contribution requirements when establishing the criteria for *de minimis* contributions.[12] It is possible, indeed likely, that the costs of complying with the Board's recommendation may be quite small. If a small carrier's cost of complying with the universal service rules, however, exceeds the amount of its contribution, it makes sense to classify those contributions as *de minimis* and to exempt that carrier from contributing. Sound public policy requires that the cost of compliance be taken into account when promulgating new rules, and TCG recommends that the Commission modify the Board's recommendation accordingly.

TCG agrees with the recommendation to base contributions on gross revenue less payments to other carriers[13] and TCG also supports the assessment of both inter- and intra-state revenue[14] for both high cost support and the support for schools and libraries. The jurisdictional separation between state and interstate telecommunications is blurring, making such distinctions more and more difficult.

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[12] *See* Recommended Decision, paragraph 799.

[13] *See* Recommended Decision, paragraph 807.

[14] *See* Recommended Decision, paragraph 817.

As a local telecommunications carrier that has built its networks city by city and state by state, TCG is sensitive to the rights of the states to develop their own means of encouraging local exchange competition. To the extent that a universal service mechanism is necessary, however, it should be truly national in scope and should reduce, if not eliminate entirely, the need for state-run funds.

Administrator

TCG supports the Board's recommendation to select an independent administrator to manage the fund.[15] TCG further agrees that the National Exchange Carrier Association is not qualified as an independent administrator and should not be considered for this role for either the schools and libraries portion of the fund or the high cost portion, even for an interim period. Although the time frame for implementing the fund for schools and libraries is relatively short, TCG believes there is sufficient time to conduct a search for a capable administrator, eliminating the need to employ NECA as an interim administrator. Such an administrator must have strong accounting competencies as the fund will function largely as a bank. Like the RFP requirement for schools and libraries, the Commission (or its designee) should initiate an RFP for a fund administrator. This approach will minimize the cost of administering the fund and ensure its independence.

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[15] *See* Recommended Decision, paragraph 829.

III. CONCLUSION.

With this Recommendation, the Joint Board has taken a giant step towards establishing a competitively neutral mechanism for maintaining and advancing universal service. Although many aspects of the recommendation will generate considerable debate, TCG is confident that the basic framework established by the Joint Board will withstand scrutiny from both legal and economic perspectives. TCG looks forward to working with the Joint Board and the Commission to hammer out the details of these recommendations over the coming months.

Respectfully submitted,

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December 19, 1996

CERTIFICATE OF SERVICE

I, Marjorie Schroeder, do hereby certify that a copy of the foregoing Comments was sent by first class United States mail, postage prepaid, this 19th day of December, 1996, to the following:

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